

INTERIM REPORT

**SUPPORTING IMPLEMENTATION OF THE
LEGAL AND REGULATORY FRAMEWORK
FOR ALBANIA'S WATER SUPPLY,
WASTE WATER, AND SOLID WASTE SECTORS**

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INTERIM REPORT

SUPPORTING IMPLEMENTATION OF THE LEGAL AND REGULATORY FRAMEWORK FOR ALBANIA'S WATER SUPPLY, WASTE WATER, AND SOLID WASTE SECTORS

1. EXECUTIVE SUMMARY

This interim report summarizes the work performed by the Contractor's Senior Legal/Regulatory Specialist in Tirana, Albania October 7 - 15, 1996. Initially, the Contractor was tasked to: 1) resolve certain jurisdictional conflicts existing between the National Water Resources Law and the National Water Sector Regulatory Act; and, 2) continue work on elaboration of the legal and administrative structure of the regulatory commission authorized under the latter act. Following consultations in the field, USAID's Resident Urban Infrastructure Advisor directed the Contractor to focus efforts on those activities identified under Task 2 of the Statement of Work.

Progress to date in developing the organizational and administrative structures of the National Water Supply, Wastewater and Solid Waste Regulatory Commission (Commission) has been hampered by the political uncertainty attendant to recent elections. With those elections now completed, and appointment of the Minister of Public Works, Territorial Adjustment and Tourism imminent, the prospects for rapid progress toward creation of a rudimentary regulatory capacity are better now than they have been since May.

The greatest constraint to progress at this point is the need for appointment of the Commission's Executive Director. Once this is accomplished, completion of Task 2 activities and associated deliverables will be possible. An important step in this process is allocation of the Commission's FY-1 budgetary resources. Follow up discussions with the Government and the World Bank will be necessary to determine whether Project Preparation Facility funds can be dedicated to this purpose.

Creation of the Commission will require an official act by the Council of Ministers. The Ministry should begin work in this direction at the earliest possible opportunity. A corporate charter, mission statement and charter of accounts will be prepared and submitted to the Government for approval. Once approved, the Commission will be registered as a corporate entity and begin formal operations.

In addition to appointment of an Executive Director, it is recommended that a Regulatory Economist also be appointed to assist the Government in developing and adopting rate methodologies, accounting standards and financial reporting and monitoring capabilities. These preparatory steps should be tied to delivery of USAID technical resources including on-the-job training and short-term technical advisory services.

The Ministry's draft National Water Services Privatization Strategy is also reviewed. The "two-track" approach adopted is consistent with the work performed to date under World Bank auspices and offers a pragmatic, step-by-step approach to addressing the challenges of Albania's smaller urban and rural water supply systems. The Ministry may consider, however, strengthening the linkage in its Strategy between privatization of water supply services and the need for an appropriate legal and regulatory framework to support that policy.

2. BACKGROUND

2.1. Effect of Recent Elections

Privatization of Albania's water supply sector is moving forward despite the political uncertainty created by recent national and local elections. President Sali Berisha's Democratic Party dominated parliamentary elections in June that were marred by reported polling irregularities. Based on early returns in recent local elections held on October 20 and 26, 1996, the Democratic Party appears to have repeated its earlier electoral success by capturing most of the 64 mayoral posts contested.

Prevailing political uncertainty has hindered the work of the recently renamed Ministry of Public Works, Tourism and Territorial Adjustment (formerly known as the Ministry of Construction and Tourism). Former Minister Albert Brojka announced in September 1996 that he would step down from his post to run for the mayor of Tirana, which he won. In his stead, the Government appointed Vice Minister Erenst Noka to serve as Acting Minister until a permanent appointment could be made. It is expected that an announcement on the appointment will be made shortly now that local elections are completed. Acting Minister Noka appears to be a strong candidate for the position although the final outcome is still uncertain.

2.2 Summary of Progress to Date

In March 1995, the Contractor assisted the Government in organizing a program to develop strategies for improving public services provision through public-private partnerships. During the succeeding months, the Government conducted discussions with USAID, the World Bank and other donor organizations concerning privatization of its water supply, wastewater and solid waste sectors. An October 6, 1995, World Bank Aide Memoire summarizes a strategy for privatization of the Tirana water system. Pursuant to an agreement reached between the Government and the World Bank, a \$500,000 Project Preparation Facility (PPF) to finance consultant services in support of the privatization process was created. As the result of a competitive selection process, a contract was awarded to KPMG (Milan) to perform services as described in the relevant Terms of Reference negotiated and agreed to by the Government, the World Bank and KPMG. During this period, and at the request of the Government, USAID agreed to provide technical assistance in support of the Government's effort to create an independent regulatory commission to provide oversight for the Tirana water system and subsequent privatizations in water supply, wastewater and solid waste service provision in Albania.

In November 1995, the Institute for Public Private Partnerships (IP3) consultants began work with the Ministry to develop a legal and regulatory framework to support privatization of Albania's water supply, wastewater and solid waste sectors. At the Government's request, the

consultants drafted two legislative acts. The first removed these activities from Albania's "negative list" for privatization. The second called for the creation of an independent regulatory commission (Commission) patterned on recognized international "best practices" to provide oversight in a post-privatization environment. For the purposes of this report, this act is referred to as the National Water Sector Regulatory Act (NWSRA).

The two draft legislative acts were submitted to the Ministry's Committees for Privatization and Regulation for comment and revision in mid-November. In early December 1995, an IP3 legal/regulatory specialist returned to Tirana to assist the Ministry in making final revisions to the legislation by a Government-imposed deadline of December 15. The deadline was met and the acts were submitted to the Government for legislative action on schedule. Work then turned to supporting the Government in developing the institutional and individual capacity necessary to implement the legal and regulatory framework for privatization of the water supply, wastewater and solid waste sectors.

In February 1996, a group of Ministry officials responsible for water privatization and associated regulatory issues attended a two-week USAID-funded training program and study tour in Washington, D.C., its environs, and Nashville, Tennessee. One objective of this program was to highlight the linkages between public services privatization and the consequent need for effective regulatory oversight. Participants received intensive theoretical and practical training in public sector privatization and regulatory economics, design and management. The second objective was to support the Ministry's effort to develop the institutional and individual capacity necessary to carry out the Government's program to privatize these essential public service sectors. To this end, a strong emphasis was placed on the practical aspects of regulating private provision of water and waste services to the public. Visits to state regulatory commissions and water service providers were facilitated with this objective in mind. In addition, detailed presentations on the practical steps necessary to establish the water sector regulatory commission were given to assist the participants in developing a practical plan to guide their work during the remainder of 1996 and into 1997. Steven Swanson, USAID's newly appointed Resident Urban Infrastructure Advisor (RUIA) to the Ministry was invited to participate in this program as a means of introducing him to his Albanian counterparts and providing an opportunity for him to familiarize himself with the Ministry's work up to that point.

On March 25, 1996, the NWSRA and companion legislation authorizing privatization of water and waste services were enacted by Parliament. On the same date, a separate piece of legislation, known as the National Water Resources Law (NWRL) was also ratified by Parliament. Among other things, the NWRL called for the creation of a National Water Resources Council (Council) to define and coordinate national water resources policy issues as well as perform many of the regulatory functions that were allocated to the Commission in the NWSRA. Passage of these two laws created a clear jurisdictional conflict between the Council and the Commission. This jurisdictional conflict was considered significant enough by the Ministry and USAID to warrant funding a short-term technical assistance intervention to assist the Government in resolving the conflict and resuming the work of defining the Commission's administrative and operational structures and procedures.

Mark Belcher, Senior Legal/Regulatory Specialist, was tasked under RFS No. 107, Contract No. EPE-0034-C-00-5115-00, to outline approaches to reconcile existing jurisdictional

conflicts between the Council and Commission (Task 1(d)) and begin work toward providing detailed recommendations for the organization and functions of the Commission (Task 2(b), (c), (d)). This report summarizes the results of this effort to date and constitutes partial completion of Deliverables 2 and 4 as identified in the Statement of Work.

3. LEGAL AND REGULATORY CONFLICTS

3.1 Existing Conflict Between Policy and Regulatory Functions

The origin of the NWRL remains obscure. One account suggests that it was drafted with assistance from an Italian water expert several years ago and subsequently shelved. During the period that the NWSRA legislation was being drafted and considered by the Ministry's Privatization and Regulatory Committees, the NWRL was not under active consideration. It appears that during the period between December 1995 when the draft legislation was submitted to the Government for parliamentary action, and late March when it was enacted, the NWRL was revived and submitted without any attempt to harmonize its provisions with the other laws under consideration.

The jurisdictional conflict that exists between the NWRL and NWSRA lies in a confusion between the policy development and coordination functions on the one hand, and independent regulatory oversight on the other. Following extensive consultations with Acting Minister Noka and his senior staff, the RUIA, Senior Legal/Regulatory Advisor Martha Beauchamps, Policy Analyst Claire Romanik and legal experts representing EU Phare and UNFAO, a consensus was developed that the NWSRA did not need to be altered to any significant degree. Instead, it was generally agreed that the most appropriate response to this legislative conflict would be to clarify the Council's role as Albania's primary water resources policy formulation and coordination body as distinct from the regulatory oversight functions of the Commission. At RUIA's direction, Martha Beauchamps was assigned the task of suggesting modifications to the NWRL consistent with the general legal and regulatory objectives of the Government. The results of this work will be presented in a separate report. Mark Belcher was directed to initiate work on Task 2 activities in the RFS. The results of this preliminary effort and recommendations for future action are summarized in this report.

3.2 Next Steps

It is recommended that the Senior Legal/Regulatory Advisors and the Utility Regulatory Specialist confer before suggested changes to the NWRL are submitted to the Ministry for evaluation and action. It is also recommended that joint consultations be organized between the Ministry's Committee on Privatization and representatives from USAID and the World Bank to review progress to date, reaffirm program objectives and divisions of responsibility and to develop a coordinated plan of action to support the Government's effort to develop and adopt a

national water sector privatization strategy that is linked to complementary regulatory objectives and requirements.

4. REGULATORY DESIGN AND IMPLEMENTATION

4.1 Summary of Progress to Date

Due in part to the political uncertainty caused by recent elections, the Ministry has yet to make significant progress toward implementation of the NWSRA. Acting Minister Noka appears strongly committed to privatization of Albania's water supply systems and has recently taken several decisive steps in this direction. First, he has dissolved the Ministry's former committees on privatization and regulation, replacing them with a steering committee that will address privatization and related regulatory issues as a single body. Acting Minister Noka chairs the Committee and Beznik Goxhaj as been appointed to serve as its Deputy Chair. The Ministries of Finance, Energy, Agriculture and Privatization are represented on the Committee, as is USAID, through RUIA's membership. Second, recent staff reassignments have been undertaken in order to streamline and focus the Ministry's efforts to develop and implement a national water supply privatization strategy. Third, the Committee has prepared a draft national water supply privatization strategy that is to be refined and submitted to the Government for approval (See Appendix E).

The most immediate obstacle to accelerating privatization and the associated regulatory effort is the lingering uncertainty concerning the ministerial appointment. If the decision on this important question is delayed significantly, progress in the regulatory area will also be delayed, or possibly reversed. Additional urgency is lent to this question by the Government's stated intention to increase water prices to approximate the cost of service provision while eliminating subsidies to water enterprises. This reform is due to be implemented in January 1997. As explained in greater detail below, it is important that some form of rudimentary regulatory capacity be in place by the time the price increases are implemented.

4.2 Phase I—Preparatory Steps

■ **Implementation Strategy.** A step-by-step implementation strategy that accounts for the relative lack of domestic individual and institutional capacity is a crucial first step in establishing the NWRC. The Ministry should be assisted in developing a work plan that will guide and inform its efforts to develop a rudimentary regulatory capacity during the next several months. This interim report is intended to provisionally address this need and will be elaborated upon with input from Ministry personnel and the Utility Regulatory Specialist. The following sections address key operational issues from a technical assistance delivery perspective.

■ **Organizational Structure.** Responsive to Task 2(c) of the Statement of Work, Appendix C contains three diagrams that chart the hypothetical organizational evolution of the Commission from its early stages to "maturity". The focus of this report, however, is on the those steps needed to establish a minimum level of institutional and individual capacity to

regulate provision of water supply services in Albania during the next twelve to eighteen months.

■ **FY-1 Funding.** During earlier discussions between the contractor, the Ministry and World Bank Representatives, an informal agreement was reached that would allow funds from the IDA Project Preparation Facility (PPF) to be allocated to covering part or all of the Commission's FY-1 budgetary needs (See generally, *World Bank Aide Memoire*, 10/06/95.). It will be necessary to revisit this question with the Ministry and World Bank representatives in order to proceed with FY-1 budgetary planning and approval.

■ **Corporate Formation.** Part II, Art. 4(1) of the NWSRA provides that the Commission be established by official act of the Council of Ministers. The Privatization Committee should initiate this process at the earliest possible opportunity. In addition to a draft decree authorizing the Commission's creation and operation, it is recommended that the Committee prepare a draft corporate charter, mission statement and charter of accounts that will be likewise submitted for approval. Work on preparing preliminary drafts of these documents can begin immediately. Once the Commission is constituted by official act, it can be registered as a corporate entity as provided for by Albanian law.

As discussed below, registration of the corporate entity will not be possible unless and until an executive director is selected. It is recommended that a budgetary allocation be made to retain private local counsel who will assist the Ministry in preparing the necessary corporate documents and registering the corporate entity. The Contractor will work closely with local counsel to ensure that both the corporate form and governance mechanisms are compatible with regulatory design considerations and the Government's broad policy objectives in this area.

■ **Preliminary Administrative Structures.** As mentioned above, the recommended preliminary administrative structure of the Commission appears in Appendix C. It emphasizes sequenced administrative growth matched to increasing demand for regulatory oversight over time. Initially, it is anticipated that the Commission will function at a minimal operational level with appointment of an Executive Director. The Contractor will work closely with the Executive Director to elaborate upon the Commission's administrative structures and operational priorities. Appointment of an Executive Director should be accomplished at the earliest opportunity and delivery of further technical assistance resources should be tied to this project milestone since proceeding without at least one permanent counterpart is unlikely to produce sustainable outputs in terms of individual and institutional capacity building.

It is recommended that a full-time appointment of a Regulatory Economist be made as soon as possible following the Executive Director's appointment. The Regulatory Economist will:

- Provide technical input to the Ministry on establishing water supply prices on a cost recovery basis;
- Address economic and financial issues concerning elimination of subsidies or possible cross-subsidization scenarios for water supply enterprises;

- Assume responsibility for collecting and managing a database containing service provision cost data for water enterprises;
- Begin developing an economic model for a uniform rate base methodology and fee structure in water service provision; and
- Coordinate with World Bank-KPMG consultants on the development and negotiation of a price and fee structure for the Tirana water system that is consistent with Government policy objectives and prevailing market conditions.

To the extent feasible under current conditions, it is recommended that technical assistance resource flows relating specifically to accounting, financial systems and rate-making be tied to the appointment of a Regulatory Economist.

It is recommended that the Commission's initial staffing be rounded out by an administrative assistant to support both the Executive Director and the Regulatory Economist in their respective duties. To the extent feasible, the Government should also consider making the appointment of the Executive Director and Regulatory Economist on an open, competitive basis according to published minimum qualifications and candidate selection factors.

4.3 Phase II—Establishing Commission Operations

■ **Preliminary Procurement.** It will be necessary for the Executive Director to make an initial determination of procurement needs as a first step in developing an FY-1 budgetary request. It is recommended that the Commission be initially located in the Ministry to achieve maximum economies and maintain close collaboration with the Privatization Committee and other Ministry counterparts. At a minimum, it is anticipated that computer equipment (including appropriate database and information management software) and communications equipment (phone and fax) will be required. The need to procure office equipment and supplies, including desks, chairs, files and room dividers will have to be determined.

It will also be necessary to establish salary rates for the Commission. It is recommended that salary rates be set at or near prevailing private sector labor rates for comparable activities.

■ **Submit FY-1 Budget for Approval.** Once completed, the Commission's provisional FY-1 budget should be submitted for approval and review by the Ministry. Appropriate measures will be undertaken to define and establish financial controls and reporting requirements prior to disbursement from the PPF or other budgetary source as implied in Task 2(b) of the Statement of Work.

■ **Register Corporate Entity.** Consistent with the requirements of relevant Albanian law, the Commission should be registered as a corporate entity at which time it will begin formal operations with appropriate corporate governance mechanisms in place. It is recommended that a budgetary allocation be made for an appropriate public awareness/education campaign to coincide with the commencement of formal operations by the Commission.

4.4 Phase III—Building Individual/Institutional Capacity

■ **On-the-Job Training.** Due to a relative lack of institutional and individual capacity, USAID may wish to provide an increased level of technical support to the Ministry and newly appointed Commission staff in the crucial period leading up to the planned water price reform. In large measure, the technical support required will be in the form of on-the-job training supplied by short-term technical advisors who have been working closely with Ministry officials on regulatory issues during the past year. Based on further assessment and evaluation, it may be recommended that USAID consider funding four-week internships for the Executive Director and Regulatory Economist with established regulatory bodies in the United States or Europe if the necessary arrangements, timing, and available technical assistance resources permit.

■ **On-Going Technical Support.** The tasks identified in this interim report are those minimally necessary to create a rudimentary regulatory capacity in response to the Government's plans to reform water services prices by early 1997. Delaying price reform, or proceeding without a provisional regulatory oversight capability, are clearly sub-optimal outcomes. It is, therefore, anticipated that additional technical assistance in the form of specialized training, technical assessments and short-term consulting assignments will be necessary to support the Government's effort to solidify and augment the rudimentary regulatory capacity that will be developed during the next several months.

As required by the NWSRA, a selection procedure for the appointment of five commissioners must be initiated within one year of passage, or by March 24, 1997. Defining and integrating the Commissioner's duties into the developing administrative and operational structures of the regulatory commission will pose significant management challenges that will require outside technical inputs. Further, it is anticipated that the demand for regulatory oversight will increase significantly as completion of the Tirana water system privatization approaches in August 1997. Given that establishing a functional regulatory capacity is integral to, and supportive of, this process, it is anticipated that Commission staff will be involved in an advisory capacity during the drafting and negotiation of the agreement between the private operator and the Government of Albania.

5. STRENGTHENING LINKAGES TO PRIVATIZATION

5.1 Commentary on the National Water Services Privatization Strategy

At Acting Minister Noka's request, this report includes a brief commentary on the Privatization Committee's draft National Water Sector Privatization Strategy. In general terms, the Strategy is consistent with international best practices and is impressive both for its comprehensive scope and pragmatism. The Committee's strategy sets forth a "two-track" strategic approach to water supply privatization that affirms the work completed to date under the auspices of the World Bank IDA PPF and outlines a sequenced approach to privatization of Albania's remaining water supply enterprises. From a technical point of view, the strategy appears to be realistic given current conditions in Albania. Finally, it seems to be a balanced approach to accomplishing the Government's economic and social objectives in privatizing water supply services in the shortest time possible.

Two observations are offered at this point. First, the Strategy does not explicitly link the privatization of public services with the need for an effective regulatory oversight capability. As suggested elsewhere in this report, the two processes should be integrally linked. Given this, the Committee may wish to strengthen and elaborate upon this point in its draft. Second, the Strategy does not explicitly identify how it will be implemented once finalized and approved. The Committee may consider specifying that the Ministry will develop subsidiary work plans for each of the two “tracks”. In these work plans, key operational issues and tasks should be identified and assigned to specific individuals or task groups. The work plans should also include a schedule of outputs with associated benchmarks and performance indicators. Finally, to the extent necessary, the Ministry should consider formulating requests for technical support geared specifically to the tasks and outputs identified in the subsidiary work plans that could be submitted to USAID, the World Bank and other donors for evaluation and negotiation.

5.2 Need for Consultations

Based on consultations with World Bank representatives in Washington, D.C. and Tirana, preparatory work on privatization of the Tirana water system appears to be on schedule. As this work proceeds, it will be increasingly important to have close collaboration between the privatization effort supported by the World Bank and the regulatory work that is being supported by USAID. (See, e.g., Appendix A) This is especially true since responsibility for monitoring compliance with the agreement between the Government and the private provider will fall to the Commission. It appears that it would be both prudent and constructive for the Ministry to facilitate closer collaboration between relevant donor organizations advisable to being working toward closer collaboration at this point so as to avoid confusion, duplication of effort and possible legal and operational conflicts.

6. CONCLUSION

At a time to be determined by the Ministry and USAID, the Contractor will field its Senior Legal/Regulatory and Utility Regulation Specialists to complete work on Task 2 activities and associated deliverables. As noted above, the precise timing and content of the work to be performed will depend to a significant degree on the Government's ability to appoint an interim Executive Director to spearhead the effort to establish the Commission as a functioning corporate body.

APPENDIX A

OVERVIEW OF USAID AND WORLD BANK SUPPORT FOR PRIVATIZATION OF THE TIRANA WATER SUPPLY SYSTEM

INSERT GRAPHIC "APPX-A.VSD"

APPENDIX B

OVERVIEW OF INSTITUTIONAL RELATIONSHIPS ENVISIONED BETWEEN THE NATIONAL WATER COUNCIL AND THE REGULATORY COMMISSION

INSERT GRAPHIC "APPX-B.VSD"

APPENDIX C

PROPOSED REGULATORY STRUCTURE OF THE REGULATORY COMMISSION

INSERT GRAPHIC "APPX-C.VSD"

APPENDIX D

TASK LIST

Component 1: Preparatory Steps

| Authority | Action Required | Tasks or Issues Implied |
|---------------------------------|---|---|
| Part II, Art. 4, Sec. 1 | Parliament adopts Act | (1) Act submitted to and approved by Council. (2) Council presents Act to Parliament for ratification. (3) Act is ratified by Parliament. |
| Part II, Art. 4, Sec. 1 | Council creates Commission by decree | (1) Complete negotiations with World Bank on Project Preparation Facility (PPF). (2) Clarify Commission's role and interest in bid and tender process, particularly relating to terms and conditions of service, base rates, rate determination methodologies and related issues. (3) Disbursement of PPF to GOA. (4) World Bank begins preparation of bid/tender documents for Tirana/Durres. (5) GOA earmarks a portion of PPF funds for creation of Commission based upon a preliminary estimate of FY-1 expenses. (6) GOA approaches Donors for additional technical assistance to support creation of the Commission. |
| Part II, Art. 4, Sec. 2 | Commission constituted as a corporate body | (1) Appoint Commission founders (Task Force) who will be responsible for implementation until Commissioners are appointed. (2) Prepare Commission foundation documents including corporate charter and charter of accounts. (3) Register corporation as a legal entity as required by law. |
| Part II, Art. 4, Sec. 4(a), (b) | Establish Selection Panel | (1) Identify, evaluate and select Panel members. (2) Provide guidelines to Panel for its work: (a) See, e.g., Part II, Art. 4 - 8, 10, 11, 12. (b) See, e.g., Part III, Art. 15. |
| Part II, Art. 4, Sec. 5 | Selection Panel presents list of nominees to Council within 2 months. | (1) Panel establishes selection process. (2) Panel solicits applications. (3) Panel evaluates and selects nominees (See, Part II, Arts. 4, 5). |
| Part II, Art. 4, Sec. 5 | Within 30 days, Council appoints Commissioner s selected from Panel's list of nominees. | (1) Disbursement of funds from PPF complete. (2) Foundation documents completed and corporation registered. (3) Decree by Council establishing pay for Commissioners (See, Part II, Art. 8). (4) Commissioners officially appointed. (5) Transfer of start-up funding to Commission. (6) Commissioners assume duties. |

Component 2: Administrative Structures

| Authority | Action Required | Tasks or Issues Implied |
|---|---|---|
| Part II, Art. 6, Sec. 1 Part II Art. 12 | Commission headquarters to be established in Tirana | (1) Prepare preliminary estimate of FY-1 resource requirements: (a) Assess space requirements for initial Commission operations: (i) Identify potential headquarters sites. (ii) Negotiate lease terms. (iii) Secure option on headquarters space. (b) Define administrative structure of Commission and prepare estimate of minimum staffing needs and associated costs (see below). (c) Prepare itemized list of equipment needed and solicit competitive price quotes. (2) Prepare detailed FY-1 budgetary request and submit to Council for approval. (3) Create relationship with reputable bank and establish necessary operating accounts (See, Part II, Art. 12, Sec 2 - pre-approval of bank by GOA required). (4) Obtain approval of FY-1 Budget and disbursement of funds into bank account. |
| Part II, Art. 6, Sec. 2 Part II, Art. 7 Part II, Art. 9 Part II, Art. 10 Part II, Art. 13 | Establish administrative rules and procedures to ensure the efficient discharge of the Commission's duties. | (1) Create administrative structures for Commission operations and management (e.g.): (a) Establish Executive Secretariat: (i) Office of the Chairman - Executive Director, whose duties include: - Personnel and Administration - Planning and Development - Facilities Management and Administrative Logistics - Controller, whose duties include: - Accounting - Internal Audit - Payroll - Financial Records - Budget - Financial Reporting - Taxes - Secretary (Agenda, Minutes, Document Control) - External Affairs (Government, Press, Consumer) (ii) Office of General Counsel (iii) Office of Administrative Hearings (b) Define functional departments and scope of authority (e.g.): (i) Office of Water Supply and Distribution - Licensing and Permitting - Rate Setting - Service, Safety and Management Efficiency Standards (ii) Office of Waste Water Treatment and Public Sanitation - Licensing and Permitting |

| Authority | Action Required | Tasks or Issues Implied |
|-----------|-----------------|---|
| | | <ul style="list-style-type: none"> - Rate Setting - Service, Safety and Management Efficiency Standards (c) Develop rule-making and adjudicative procedures (see Component 2) (d) Establish rate determination methodologies (see Component 3) (2) Prepare Commission's organizational chart. (3) Develop job descriptions and lines of authority for key positions. (4) Draft and adopt Commission's internal operating rules and procedures. |

Component 3: Rule-making and Adjudicative Procedures

| Authority | Action Required | Tasks or Issues Implied |
|------------------------------|---|--|
| Part III, Art. 14 | GOA has power to issue directives on water supply, waste water and sanitation policy. | <p>(1) Establish liaison with relevant elements of GOA to monitor and advise on policy matters relating to water supply, waste water treatment and public sanitation.</p> <p>(a) Clarify or assert Commission's:</p> <p>(i) Role as an independent regulatory body.</p> <p>(ii) Jurisdiction over national and local regulatory matters.</p> <p>(iii) Relationship to other branches of government.</p> <p>(b) Establish clear division between national and local regulatory authority and mechanisms for coordinating regulatory initiative on both levels.</p> <p>(2) Clarify procedures by which the Commission can challenge GOA policies that conflict with Act by submitting the matter to the Constitutional Court.</p> <p>(a) What constitutes a "conflict"?</p> <p>(b) What jurisdictional requirements are imposed by Court before it will hear a case?</p> <p>(c) What Commission actions are reviewable by the Court?</p> <p>(d) What are the procedural requirements for bringing a controversy to the Court?</p> |
| Part III, Art 16, Sec. 1 (a) | License commercial entities engaged in business activities within the jurisdiction of the Commission. | <p>(1) Define classes and categories of business activities that are required to operate under license.</p> <p>(a) Water supply - above ground, subsurface, transported.</p> <p>(b) Water distribution through existing systems.</p> <p>(c) Solid waste disposal.</p> <p>(2) Define the scope of geographic or subject matter regulatory activity (e.g., Tirana and Durrës) during the start up period and develop a plan to expand scope of Commission's activities over time.</p> <p>(3) Establish minimum qualifications for licensees consistent with Part III, Art. 18.</p> <p>(a) Operational capabilities.</p> <p>(b) Financial capabilities.</p> <p>(c) Industry experience.</p> <p>(d) Integrity.</p> <p>(e) Domicile.</p> <p>(4) Adopt procedures for license applicants and prepare standard license application forms.</p> <p>(a) Information required from applicant.</p> <p>(b) License fee charged.</p> <p>(c) Amount of time for preliminary determination.</p> <p>(5) Create administrative procedures for evaluating and verifying license applications.</p> <p>(a) Establish administrative point of contact for applicants (e.g., Commission Clerk's Office) to carry out preliminary review process (e.g., applicant qualifications, required information, fee paid).</p> <p>(b) Develop review process resulting in formal recommendations</p> |

| Authority | Action Required | Tasks or Issues Implied |
|--|--|---|
| | | <p>on license applications.</p> <p>(6) Draft and adopt standard license agreement language.</p> <p>(7) Provide an open and transparent process for granting license applications including the opportunity for public notice and comment.</p> <p>(8) Provide an open and transparent process for denying or revoking licenses including an opportunity for administrative review of the negative determination.</p> <p>(9) Develop administrative oversight mechanisms to verify compliance with license terms and conditions.</p> |
| Part III, Art. 16, Sec. 1 (b) | Approve prices or charges and terms and conditions of services provided by licensees in the Water Supply Sector. | <p>(1) Develop an administrative process (e.g., application, public notice, hearing, public comment, administrative appeal) for reviewing applications for rate increases or service changes.</p> <p>(a) Establish an official point-of-contact with the Commission (e.g., Commission Clerk, Office of the Executive Director) for receiving requests for official action and providing notice of impending or completed official acts of the Commission.</p> <p>(b) Establish mechanisms for information gathering, organization, storage and retrieval (including public record).</p> <p>(c) Create administrative procedures for processing applications, complaints and other requests for official action.</p> <p>(i) Classify action requested.</p> <p>(ii) Assign file number and register in official docket.</p> <p>(iii) Forward to appropriate administrative office for evaluation and preliminary recommendation.</p> <p>(d) Develop procedures for formal and informal hearings and preparation of official record.</p> <p>(e) Define administrative review procedures for informal determinations.</p> <p>(f) Clarify judicial scope of review and appellate procedure (see above).</p> <p>(2) Develop rate determination methodologies (see Component 3).</p> <p>(3) Create standards for evaluating and acting on rate increase/service change requests.</p> |
| Part III, Art. 16, Sec. 1 (c); Part V, Art. 25 | Develop procedures and standards for investment and sale of assets in the regulated sector. | <p>(1) Create industry-specific standards for investment, capacity upgrade, safety, service and management efficiency (See, Part V, Art. 28).</p> <p>(2) Establish guidelines and administrative procedures for investment (capacity expansion or upgrade) of regulated business activities.</p> <p>(3) Develop guidelines and administrative process (e.g., application, public notice, hearing, public comment, administrative appeal) for reviewing proposed sales of assets or assignment of license rights in regulated sectors.</p> |
| Part III, Art. 17, 18, 19, 20, 21, 22 | Regulated businesses to be licensed | See above re definition of regulated business activities and licensing requirements. |

| Authority | Action Required | Tasks or Issues Implied |
|---|--|--|
| | for operation. | |
| Part III, Art. 15, Sec. 2 | Commission shall arbitrate disputes arising between licensees. | Create a dispute resolution mechanism within each of the functional departments created and adopt streamlined arbitration practices and procedures. |
| Part V, Art. 25, 26, 27, 28; Part VI, Art. 30, 33 | Commission orders to be enforced. | (1) Establish administrative capability to receive and process complaints brought by or on behalf of consumers of regulated services (including ombudsman function). (2) Establish standards of compliance with Commission orders and directives. (3) Create administrative structures to investigate and make preliminary recommendations concerning possible violation of Commission orders or directives, and fulfill statutory reporting requirements. (4) Clarify enforcement mechanisms and powers. |

Component 4: Rate-making and Accounting Procedures

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| | | <p>Select Uniform System of Accounts</p> <ul style="list-style-type: none"> (1) Ease of application - simplicity. (2) Widespread use - Europe. (3) "Suitability" for current and projected needs: <ul style="list-style-type: none"> - Appropriate for infant industry? - Cross-sectoral applicability? |
| | | Adapt to Albanian Circumstances. |
| | | Assign Responsibility for Function w/in the Commission. |
| | | Adopt and Publish Standards. |
| | | Develop Training and Technical Support Programs for Industry. |
| | | Develop Audit and Compliance Monitoring Capabilities. |
| | | <p>Regulating Industry Accounting Practices</p> <ul style="list-style-type: none"> (1) Assess Current Capabilities: <ul style="list-style-type: none"> - Accounting/Finance Expert to Spearhead Effort? - Manpower Resources Sufficient to Task? (2) Assign Responsibility for Developing a Uniform System of Accounts to Specific Individuals. (3) Identify Areas Where Outside Expertise Will be Needed. (4) Develop Time-Line (Specific Results by a Specific Date). (5) Establish Internal Reporting/Monitoring Relationships. |
| | | Determine the Rate Base (Value of Utility's Property - Accrued Depreciation) |
| | | <p>Data Collection - Collect existing data and studies</p> <ul style="list-style-type: none"> (1) Elements of Value = Tangible + Intangible Assets "Used and Useful" in providing regulated goods or services |
| | | <p>Establish Measures of Value</p> <ul style="list-style-type: none"> (1) Construction Cost Value = Original, Book, Prudent Investment or Capitalization Cost (2) Reproduction Cost Value = Current, Split, Tax Assessment, Market, Purchase. |
| | | <p>Develop Methodology</p> <ul style="list-style-type: none"> (1) What is included in the rate base. (2) What is excluded from rate base. (3) What method (or measure) of value will be applied. |
| | | <p>Adjust for Realities and Implement</p> <ul style="list-style-type: none"> (1) Develop test cases. (2) Adjust model to account for political and operational realities. (3) Assign Responsibility for Function w/in the Commission. (4) Formally Adopt and Publish Standards. (5) Develop Training and Technical Support Programs for Industry. |

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| | | (6) Develop Audit and Compliance Monitoring Capabilities. |
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APPENDIX E

DRAFT WATER PRIVATIZATION STRATEGY

REPUBLIC OF ALBANIA MINISTRY OF PUBLIC WORKS, TERRITORIAL ADJUSTMENT AND TOURISM

REPORT OF THE COMMITTEE ON PRIVATIZATION:

A PROPOSED NATIONAL STRATEGY FOR PRIVATIZATION OF ALBANIA'S WATER SUPPLY SECTOR

INTRODUCTION

Taking into account the importance of a clean and dependable supply of water to the social and economic development of Albania, the Government has placed a high priority on developing a privatization strategy for the water supply sector that will:

1. Attract foreign investment, technology and management skills in water supply services;
2. Improve the quality, dependability and scope of water service throughout Albania; and,
3. Balance the need for rapid economic development with concerns for the social welfare of all citizens of Albania.

The Ministry of Public Works' Committee on Privatization has been directed to develop a practical approach to the complex problems of privatization of public water supply that will meet the Government's objectives stated above. This document summarizes the Committee's conclusions and provides a plan for a three-year program of work that should be pursued to achieve the Government's objectives.

Following an overview of the problem facing the Government and relevant experiences to date, a two-track strategic approach is proposed. The first track, already underway, focuses on privatization of the Tirana and Durres water supply systems through an international competitive tender with support from the World Bank and USAID. The second track of this strategy addresses the more difficult problem of improving operational efficiency in the remaining forty-two water service providers throughout Albania. Finally, the need for, and

anticipated role of, an independent regulatory body will be discussed in relation to the privatization strategy proposed in this report.

OVERVIEW OF THE PROBLEM AND EXPERIENCES TO DATE

The quality, dependability and scope of efficient water supply in Albania are inadequate and must be improved if the economic and social welfare of its citizens are to be increased to the level of the rest of Europe. The first objective of the Government is to improve the quality and reliability of water service so that clean, safe water will be supplied to users 24 hours a day at pressures sufficient to reach the upper floors of typical apartment blocks and commercial buildings.

The second objective of the Government is to create incentives for the efficient use and allocation of water throughout Albania. For many years, the Government has subsidized the price of water paid by the consumer. In addition to creating a large financial drain on public finances, this practice has led to wasteful and inefficient use of water and a decline in the quality of service to consumers. To remedy this situation in the shortest time possible, the Government has determined that the price of water charged to the consumer must reflect the actual cost of providing that service. This will help:

1. Reduce the strain the national budget created by continued government subsidy of water supply;
2. Create the conditions necessary for private companies to provide economically efficient and socially responsible water supply services to consumers under carefully determined conditions; and
3. Introduce into practice in Albania the internationally recognized principle that among particular classes of consumer (e.g., industrial, residential, agricultural) the amount paid for water should reflect the cost of providing water per unit (M3) multiplied by the actual amount of metered water usage.

It is recognized that these reforms imply a fundamental change in how water is supplied to consumers in Albania. Managing this change successfully will be extremely difficult during the early stages of the Government's program. In the short-run, the reforms will create additional hardship for citizens already experiencing difficult times. The challenge for the Government will be to implement the reforms as quickly and as efficiently as possible.

Empirical studies in other nations have demonstrated consumers are willing to pay higher prices for water as long as there is a comparable increase in the quality of service. The trade-off between increased price and improved service, however, is not immediate. Albania's water supply infrastructure is in need of extensive upgrading and rehabilitation before service to consumers can be increased appreciably. This will require both time and significant levels of investment. It is the Government's intention and responsibility when undertaking these reforms

to ensure that, consistent with the objectives stated above, the benefits of improved service are realized in the shortest time possible under current economic and social circumstances.

Experience to date in developing and implementing a national strategy for privatization of Albania's water supply systems has been generally satisfactory. Nevertheless, given the size and complexity of the challenge, and the urgent need to rapidly improve water supply services, it is useful to review progress to date, identify priorities and develop a strategy that will build upon work performed to date and accelerate reform in this area.

The first concrete steps toward reform in this sector began in early 1995 when the Government entered into discussions with the World Bank and USAID about reform strategies for water supply. In March 1995, a Memorandum of Understanding was concluded with USAID. Under this agreement, foreign consultants (PADCO and Institute for Public Private Partnerships) conducted technical training in Tirana. The program was designed to assist Ministry officials in developing an initial policy approach and work plan to promote urban infrastructure investment and development in Albania.

Considering the work performed in March 1995, a World Bank mission visited Tirana in June and October 1995 to discuss strategies to promote private involvement in water supply in Albania and how that strategy could be supported by World Bank funds. World Bank representatives and USAID consultants made the following recommendations to the Government:

1. That private involvement in Albania's water supply sector will be introduced through a two-stage approach that would begin with a management contract or concession agreement that would be phased into partial equity ownership ("strategic partnership") over time.
2. That the process of privatization begin with corporatization - the legal transformation of state-owned water enterprises into corporate entities as provided for by Albanian law.
3. That the Government identify some triggers that would eventually lead to high levels of private involvement in providing water supply in Albania.
4. That an appropriate legal and regulatory framework be in place at or before the pilot privatization is completed.

The World Bank proposed (and the Government agreed to) an IDA loan of \$500,000 to fund consulting services to support the Government's effort to prepare and launch an international tender for foreign participation in the Tirana and possibly Durres water systems. In early 1996, the Government's request for IDA funds was approved by the World Bank and a Project Preparation Facility (PPF) was established. The consultant selection process was completed in March 1996 with KPMG (Italy) selected to perform necessary pre-privatization services on behalf of the Government. KPMG consultants began work on the project in July 1996.

At present, KPMG consultants are working to complete the following tasks necessary to launch an international tender for the Tirana water supply system:

1. Prequalification of potential strategic investors;
2. Preparation and implementation of corporatization of the Tirana system;
3. Preparation of a draft privatization strategy for the Tirana system and necessary tender documents;
4. Organization of a pre-bid visit and conference;
5. Finalization of tender documents and privatization strategy;
6. Issuance of tender documents and evaluation of bids; and,
7. Supporting the Government in negotiations with competitive bidders.

While precise dates for the completion of each of these tasks are not available, it is planned that the entire process will be completed by August 1997.

Throughout this period (March 1995-present), USAID has supported the Government in its efforts to develop and implement a comprehensive policy toward improving urban infrastructure and related services. Through a combination of long- and short-term technical advisors and specialized training, USAID has supported the Government in developing appropriate policy responses combining public-private partnerships, tailored legal/regulatory frameworks and related technical interventions (e.g., asset valuation, accounting systems).

As mentioned above, preliminary decisions concerning the appropriate regulatory model for Albania began in early 1995. In November of that year, a team of three legal/regulatory specialists visited Tirana to support the Ministry's privatization and regulatory committees in drafting laws:

1. Authorizing privatization of water supply, wastewater and solid waste services in Albania; and,
2. Creating an independent regulatory body responsible for protecting the public interest in the private provision of water supply, wastewater and solid waste services in Albania.

These laws were submitted to the Council of Ministers in December 1995 and later enacted into law in March 1996.

In addition, USAID consultants also provided technical support to the Government in drafting and harmonizing the following related supporting laws:

1. National Water Resources Law;
2. Law on Concessions;

3. Law on Procurement; and,
4. Law on Corporatization.

All of these statutes were endorsed by the Council of Ministers and enacted in law by Parliament.

Technical support in legislative drafting has also been supported by USAID through specialized technical training both in Albania and the United States. This input included a February 1996 study tour to adapt international "best practices" to Albania's specific and pressing needs. Issues concerning water enterprise organization, staffing, and operation of regulatory commissions who protect the public interest with respect to performance monitoring, tariff setting, consumer protection and environmental impact were addressed. At the conclusion of the U.S. study tour, Ministry participants began preparing an action plan for follow-up initiatives that form the basis for this proposed strategy. This report is intended to incorporate the lessons of experience learned to date and provide a logical and pragmatic approach to making the transition from public to private ownership and operation of water supply enterprises.

A TWO-TRACK STRATEGIC APPROACH

Overview

As discussed above, progress toward privatization of the Tirana water supply system is underway and is expected to be substantially complete by August 1997. This effort represents the first-track of a "two-track" strategic approach that focuses on attracting leading international water service companies to invest in and operate Albania's largest water supply systems - Tirana and Durrës. A truly national strategy, however, must also address the more complex and difficult question of how to improve water supply services throughout Albania.

The need for a "two-track" strategy is based on a frank acknowledgment that many of Albania's remaining water supply systems are probably too small in size and require too much investment to attract serious interest by world-class service providers in the near-term. Instead, it is necessary to focus on those initiatives that water enterprises, jointly or independently, can undertake that will help:

1. Improve service to consumers;
2. Increase operational and allocational efficiencies; and,
3. Attract domestic and foreign investment needed for infrastructure rehabilitation over the near- to medium-term.

It is intended that both tracks of this two-track strategic approach will be carried out simultaneously and in a coordinated fashion. Nevertheless, it is envisioned that they will be pursued independently allowing the Government, with support from the international donor community, to address those areas and problems where rapid improvements are both realistic and of immediate benefit to the largest number of consumers possible.

First Track: International Tender for Tirana

As discussed above, World Bank consultants are currently refining a strategy for the privatization of the Tirana (and possibly Durrës) water supply system and performing the necessary technical studies to launch an international competitive tender for private involvement in the sector. As a result, the "first-track" of this strategy is not discussed and will be evaluated when it is received by the Privatization Committee later in 1996 or early 1997.

Second Track: Step-by-step Pragmatism

Successful privatization of the remainder of Albania's water supply systems is hindered by several critical shortages:

1. Lack of appropriate enterprise corporate structures and well-developed legal institutions;
2. Lack of commercial technical and management skills and associated commercial experience;
3. Lack of investment capital to upgrade and rehabilitate existing water supply systems;
4. Lack of effective regulatory institutions;
5. Anticipated resistance by local officials, water system managers and employees to a significant change in the status quo; and,
6. Anticipated resistance by consumers to increased prices over the short-term as service standards are improved.

The second-track of this strategy will address each of obstacles identified above to create the proper environment for private ownership and management of water supply systems **where market conditions permit**. It should be stressed that while a common strategy is useful for planning and efficiency purposes, it is no substitute for a pragmatic approach based on a critical and objective evaluation of local conditions. In certain cases, it is likely the significant progress will take considerable time and effort to achieve.

From a strategic perspective, the "second-track" of this approach include the following mutually supporting steps:

■ **Data Collection** (November 1996-March 1997)

1. Complete a study that will provide reliable data on the cost of providing water for each of the Albania's water supply systems;
2. Gather information needed to prepare all water supply enterprises for corporatization; and,
3. Conduct an operational study to determine the extent to which operational and allocational efficiencies from economies of scale and scope can be realized by grouping enterprises into district or regional water service companies.

■ **Corporatization** (March-June 1997)

Initiate and complete the legal transformation of Albania's water supply systems into the appropriate corporate forms authorized by law.

■ **Commercialization/Restructuring** (March-December 1998)

1. Identify three to five corporatized water supply systems for inclusion in a pilot commercialization effort. The focus of this effort will be to develop and implement efficient and accountable commercial management and operations systems that can be adopted by the remaining corporatized water supply systems.
2. Carry out industry restructuring through consolidation or other appropriate measures that are:
3. Justified by potential efficiency gains;
4. Consistent with Government regulatory and social objectives; and,
5. Supported by quantitative data.

■ **Privatization** (January 1998-December 1999)

Fully or partially privatize water **enterprises where market demand for shares exists** either through mass privatization, special offerings or on a case-by-case basis as circumstances and investor interest warrants.

■ **Regulatory Oversight** (Present-December 1999)

When, and as needed, expand institutional capacity of regulatory oversight bodies (e.g., Water Supply, Wastewater and Solid Waste Regulatory Commission, Ministry of Environment) to exercise appropriate regulatory oversight functions of water supply enterprises.

■ **Public Education and Awareness** (Present-December 1999)

The success of this strategy—which calls for a fundamental change in the relationship between the service provider (government) and the consumer—will ultimately depend upon the public's perception of the economic and social benefits that these reforms promise. Simply stated, the public appreciates that:

1. There is an explicit trade-off between low prices and improved service;
2. The Government will act to protect the public interest by ensuring that increased water prices today will lead to improved service over time;
3. The Government is working to overcome the effect of decades of infrastructure neglect while constrained by with limited financial resources. Public expectations must not exceed the Government's capacity to deliver improvements in the near-term; and,
4. To succeed in this reform effort, the Government will need to wage a coordinated and sustained effort to inform and educate the public throughout the life of this project.

CONCLUSION

The broad strategic objectives identified above are **difficult to achieve even under the best of circumstances**. To succeed, the Government must devote all available resources and attention to the success of this effort. In pursuing this ambitious course, Albania cannot go it alone. During this transition period, it will be necessary to seek out technical and financial support from the international donor community; particularly from those organizations and individuals who have practical experience in Albania and who understand the unique challenges that Albania faces.

Next steps for this effort could include:

1. Adoption of a national strategy for privatization of a national water supply services;
2. Develop detailed work plans, task lists and budgetary estimates for carrying out the national strategy (outlined in this report) for privatization of Albania's water supply services;
3. Identify specific areas or subjects where competent Government personnel can carry out tasks and functions without donor assistance;
4. Identify specific areas or subjects where international donor support will be most needed and useful to accomplishing Government policy objectives, recognizing that donor resources are limited and competition for those resources is intense;
5. Initiate a new round of consultations with the international donor community to:

(a) Discuss Albania's water supply privatization strategy and necessary and useful ways to strengthen and improve it;

(b) Develop a consensus on how best to support, implement and coordinate the Government's policy initiatives for improving efficiency in the water supply sector;

(c) Develop concrete (financial) support for Albania's urban infrastructure development and reform efforts among the international donors; and,

(d) Explore specific complementary Government/donor initiatives in the areas of urban infrastructure and services including waste water, solid waste disposal and other essential services.